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In the

Supreme Court of the United States

October Term, 1993

NORMAN W. SWANSON, *et al.*,
Class A Petitioners,

and

CHARLES L. BERRY, *et al.*,
Class B Petitioners,

v.

THE STATE OF NORTH CAROLINA, *et al.*,
Respondent.

Petition for A Writ of Certiorari To The Supreme Court of North Carolina

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BRIEF IN OPPOSITION

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37 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

INTRODUCTION 1

STATEMENT OF THE CASE 3

REASONS WHY THE WRIT SHOULD NOT BE GRANTED 9

I. THE PETITION SHOULD BE DENIED BECAUSE THE NORTH CAROLINA SUPREME COURT CORRECTLY APPLIED THIS COURT'S DECISIONS IN *McKESSON* AND *HARPER* IN DETERMINING THAT PETITIONERS WERE NOT DEPRIVED OF DUE PROCESS WHEN THEIR REFUND CLAIMS WERE DENIED FOR FAILURE TO MEET THE PROCEDURAL REQUIREMENTS OF NORTH CAROLINA'S REFUND STATUTE, N.C. GEN. STAT. § 105-267. 10

1. N.C. Gen. Stat. § 105-267 met the requirements of due process by providing Petitioners with the opportunity to obtain meaningful backward-looking relief in the form of refund of taxes paid on their federal pension income in 1988. 10

2. The Supreme Court of North Carolina correctly declined to give preclusive effect to a preliminary jurisdictional finding by the District Court in Petitioners' federal litigation. 21

II. AS TO CLASS B PLAINTIFFS' CLAIMS, THE PETITION SHOULD BE DENIED FOR THE ADDITIONAL REASON THAT THE FORMER STATUTORY INCOME TAX BENEFIT FOR NATIONAL GUARD MEMBERS WAS NOT DISCRIMINATORY TAXATION IN VIOLATION OF THE PUBLIC SALARY TAX ACT OR CONTRARY TO THIS COURT'S DECISION IN *DAVIS V. MICHIGAN DEPARTMENT OF TREASURY*. 24

CONCLUSION 27

APPENDIX 1a

TABLE OF AUTHORITIES

CASES

Bailey v. North Carolina, 330 N.C. 227,
412 S.E.2d 295 (1991), *cert. denied*, 504 U.S. ___,
112 S. Ct. 1942, 118 L. Ed. 2d 547 (1992) 5

Barker v. Kansas, 503 U.S. ___,
112 S. Ct. 1619, 118 L. Ed. 2d 243 (1992) 3

Bob Jones University v. Simon,
416 U.S. 725 (1974) 15

Coca-Cola v. Coble, 293 N.C. 565,
238 S.E.2d 780 (1977) 5, 11

Davis v. Michigan Department of Treasury,
489 U.S. 803 (1989) 1, 3, 26

Dodge v. Osborn, 240 U.S. 118 (1916) 15

Edelman v. Jordan, 415 U.S. 651 (1974) 23

Green v. Mansour, 474 U.S. 64 (1985) 23

Harper v. Virginia Department of Taxation,
509 U.S. ___, 113 S. Ct. 41,
125 L. Ed. 2d 74 (1993) 9

Kirkpatrick v. Currie, 250 N.C. 213,
108 S.E.2d 209 (1959) 5, 20

Kremer v. Chemical Construction Corp.,
456 U.S. 461 (1982) 24

Matthews v. Eldridge, 424 U.S. 319 (1976) 15

McKesson v. Florida Division of Alcoholic Beverages and Tobacco, 496 U.S. 18 (1990) 9, 15, 16

Parson's Steel Inc. v. First Alabama Bank, 474 U.S. 518 (1986) 24

Perpich v. Department of Defense, 496 U.S. 334 (1990) 25

Phillips v. Commissioner, 283 U.S. 589 (1931) 15

Richmond & Danville R.R. Co. v. Reidsville, 109 N.C. 494, 13 S.E. 865 (1891) 5

Rosewell v. LaSalle National Bank, 450 U.S. 503 (1981) 18

Swanson v. North Carolina, 509 U.S. ___, 113 S. Ct. 3025, 125 L. Ed. 2d 713 (1993). On remand 9

Swanson v. North Carolina (I), 329 N.C. 576, 407 S.E.2d 791 (1991) 8

Swanson v. North Carolina (II), 330 N.C. 390, 410 S.E.2d 490 (1991) 9

Swanson v. North Carolina (III), 335 N.C. 674, 441 S.E.2d 537 (1994) 2, 5, 6, 9, 12, 14, 20, 23

Swanson v. Powers, 937 F.2d 965 (4th Cir. 1991), *cert. denied*, ___ U.S. ___, 112 S. Ct. 871, 116 L. Ed. 2d 777 (1992) 2, 4, 7, 18, 20, 22, 26

STATUTES

Public Salary Tax Act of 1939, 4 U.S.C. § 111 3

Tax Injunction Act, 28 U.S.C. § 1341 21

42 U.S.C. § 1983 7

N.C. Gen. Stat. § 105-141(b)(25) 4

N.C. Gen. Stat. § 105-151.20 6

N.C. Gen. Stat. § 105-267 . . . . . 4, 5, 6, 8, 9, 10, 11, 12, 15, 16, 17, 18, 19, 20, 21, 22, 27

N.C. Gen. Stat. § 127A-16 25

N.C. Gen. Stat. § 127A-105 25

N.C. Gen. Stat. § 127A-106 25

N.C. Gen. Stat. § 134.6(b)(4) 4

1989 N.C. Sess. Laws, ch. 792, § 1.1 3

1989 N.C. Sess. Laws, ch. 984, § 6 6

1989 N.C. Sess. Laws, ch. 1002 (1990) 4

Sup. Ct. R. 15.1 2

MISCELLANEOUS

Lawrence H. Tribe, *American Constitutional Law*, § 10-14 at 720-21 (2d ed., 1988) 15

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BRIEF IN OPPOSITION

INTRODUCTION

Petitioners' Statement of the Case is biased and argumentative and wrongly characterizes the actions taken by North Carolina public officials in response to this Court's decision in *Davis v. Michigan Department of Treasury*, 489 U.S. 803 (1989), as a concerted effort

to deprive them of tax refunds. Petitioners also inappropriately included in their appendix materials[1] that were not before the North Carolina Supreme Court when it decided *Swanson v. North Carolina (III)*, 335 N.C. 674, 441 S.E.2d 537 (1994), the decision precipitating this petition. To correct the resulting unfairness, North Carolina is compelled, pursuant to Rule 15.1, to present its own statement of the case.[2]

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[1] For example, included in their appendix are letters from federal officials to Petitioners' counsel, dated March 2 and March 8, 1994 (Petitioners' Appendix S, A173-A175); press releases and newspaper articles, dated May 13, 1994 (Petitioners' Appendix Z, A233-234) and March 10, 1994 (Petitioners' Appendix AA, A235); and a summary chart Petitioners prepared which includes self-serving entries such as the one stating that "Georgia and Virginia are struggling toward settlement." (Petitioners' Appendix CC, A238).

[2] Respondents made similar mischaracterizations when the Court of Appeals for the Fourth Circuit reviewed the Secretary of Revenue's qualified immunity defense in *Swanson v. Powers*, 937 F.2d 965 (4th Cir. 1991), *cert. denied*, ___ U.S. ___, 112 S. Ct. 871, 116 L. Ed. 2d 777 (1992). That decision is instructive because the Court of Appeals rejected Respondents' one-sided version of North Carolina's response to *Davis*. *Powers*, 937 F.2d at 971-72.

STATEMENT OF THE CASE

On March 28, 1989, this Court invalidated Michigan's laws which afforded more favorable income tax treatment to retired state employees' pensions than to retired federal employees' pensions. *Davis v. Michigan Department of Treasury*, 489 U.S. 803 (1989). The Court held that such differential tax treatment discriminated against federal retirees based solely on the federal source of their pensions in violation of the doctrine of intergovernmental tax immunity and the Public Salary Tax Act of 1939, 4 U.S.C. § 111. When *Davis* was decided, North Carolina exempted from state income taxation all retirement income of state and local government employees and teachers but exempted only $3,000 of federal pension income. After *Davis*, North Carolina equalized the tax treatment of state and federal pensions, retroactive to January 1, 1989, by repealing the tax exemption for state retirement benefits and enacting a $4,000 exclusion for the retirement benefits of both state and federal employees. (1989 N.C. Sess. Laws, ch. 792, § 1.1). Class A Petitioners are federal civil service and military pensioners[3] who seek refund of state income taxes paid on their pre-*Davis* federal pension income.

At the time of the *Davis* decision, North Carolina also excluded from state income taxation the first $1,500

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[3] For income tax purposes, North Carolina did not draw a distinction between federal civil service and military pensions. *See Barker v. Kansas*, 503 U.S. ___, 112 S. Ct. 1619, 118 L. Ed. 2d 243 (1992).

of the service pay of North Carolina National Guardsmen[4] but conferred no comparable benefit on federal military reservists or active duty personnel who paid North Carolina state income taxes. Class B Petitioners are active duty and reserve members of the federal armed forces who seek refund of taxes paid on their military service pay because they did not receive the tax benefit extended to members of the North Carolina National Guard.

Respondents are the State of North Carolina, the Secretary of the North Carolina Department of Revenue, and the State Treasurer.

Within days after the *Davis* decision, the Secretary of Revenue sought an opinion from the North Carolina Attorney General regarding the effect of *Davis* on the State income tax system and the proper procedure for refunding unconstitutional taxes. On April 10, 1989, the Attorney General advised the Secretary that all persons who met the requirements of the pertinent North Carolina tax refund statute, N.C. Gen. Stat. § 105-267, were entitled to refunds. The Secretary of Revenue then issued a press release announcing the Department of Revenue would issue refunds accordingly. *See Powers*, 937 F.2d at 971-72.

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[4] N.C. Gen. Stat. § 105-141(b)(25). This exclusion was made a tax deduction for tax year 1989, N.C. Gen. Stat. § 134.6(b)(4), and repealed effective January 1, 1990. (1989 N.C. Sess. Laws, ch. 1002 (1990)).

N.C. Gen. Stat. § 105-267[5] provides that a taxpayer challenging the constitutionality of a tax must pay the tax and protest its legality by demanding a refund within 30 days of payment. The taxpayer then has three years within which to bring suit if the Secretary of Revenue denies the demand or takes no action on it within 90 days. N.C. Gen. Stat. § 105-267 and its predecessor statutes have been in place for over 100 years. The Supreme Court of North Carolina has held that it is the exclusive method by which a taxpayer can challenge the constitutionality of a State tax statute and obtain a refund of taxes paid under that statute. *Swanson III*, 335 N.C. at 680, 441 S.E.2d at 541; *see also Bailey v. North Carolina*, 330 N.C. 227, 235, 412 S.E.2d 295, 300 (1991), *cert. denied*, 504 U.S. ___, 112 S. Ct. 1942, 118 L. Ed. 2d 547 (1992) (Applying N.C. Gen. Stat. § 105-267 to deny claims of State pensioners that taxation of their retirement benefits pursuant to a statute equalizing the tax treatment of State and federal pension income following *Davis* violated their constitutional rights); *Coca-Cola v. Coble*, 293 N.C. 565, 238 S.E.2d 780 (1977) (N.C. Gen. Stat. § 105-267 is the exclusive method to challenge the constitutionality of a State tax statute, and failure to meet its requirements bars refund claim); *Kirkpatrick v. Currie*, 250 N.C. 213, 108 S.E.2d 209 (1959) (N.C. Gen. Stat. § 105-267 accords taxpayer due process of law and is constitutional); and *Richmond & Danville R.R. Co. v. Reidsville*, 109 N.C. 494, 13 S.E. 865 (1891) (Failure

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[5] The text of N.C. Gen. Stat. § 105-267 is set out in Respondents' Appendix at page 1a.

to demand refund of tax within 30 days of payment pursuant to predecessor statute to N.C. Gen. Stat. § 105-267 bars claim for refund of tax collected pursuant to an allegedly unconstitutional statute).

Many federal pensioners met the requirements of N.C. Gen. Stat. § 105-267 and received refunds of taxes paid on their 1988 federal pension income. As of February 19, 1990, North Carolina had honored 12,404 such claims and refunded a total of $9,145,523.92. *Swanson III*, 335 N.C. at 682 n. 1, 441 S.E.2d at 542 n. 1. For those federal pensioners who failed to make timely refund demands because *Davis* was decided so near the April 17, 1989 filing deadline, the North Carolina General Assembly enacted a special tax credit permitting them to recover over a period of three years the taxes paid on their 1988 federal pension income. (1989 N.C. Sess. Laws, ch. 984, § 6, codified as N.C. Gen. Stat. § 105-151.20). *See Swanson III*, 335 N.C. at 687-88 n. 3, 441 S.E.2d at 545 n. 3. Thus, federal pensioners received either a refund or a tax credit for state taxes paid on their 1988 federal pension income.[6]

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[6] Petitioners' refund claims are limited to taxes paid on their 1988 federal pension income and cannot include previous years. Failure to protest within 30 days after paying the tax due for any year extinguishes a refund claim for that year. By the express words of N.C. Gen. Stat. § 105-267, a protest in later years cannot revive an extinguished claim since the belated protest would not come within "30 days after payment" of "the tax paid"

(continued...)

On April 14, 1989, barely two weeks after *Davis*, Class A Petitioners sued Respondents (except the State of North Carolina) for declaratory and injunctive relief and damages under 42 U.S.C. § 1983 in the United States District Court for the Eastern District of North Carolina. Relying on *Davis*, they alleged that the State officials had unconstitutionally collected income tax on their federal pension income. Class B Petitioners were allowed to join the action as plaintiffs early in 1990. All Petitioners' claims for damages were dismissed in August 1990, except for claims against the Secretary of Revenue in her individual capacity. As to those claims, the District Court rejected the Secretary's qualified immunity defense. The United States Court of Appeals for the Fourth Circuit reversed, holding that the individual claims against the Secretary of Revenue should also have been dismissed. *Powers*, 937 F.2d at 971, 973. On May 6, 1994, the District Court granted summary judgment for the Respondents on all remaining claims. (Petitioners' Appendix H, A79-A88).

On March 16, 1990, Petitioners sued the Respondents in state court for tax refunds in excess of

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[6](...continued)
in the earlier year. Therefore, if a federal retiree in 1989 timely protested the payment of state tax on his 1988 pension income, his cause of action would be limited to a refund of 1988 taxes, and he would have a three-year limitations period within which to file his action to recover a refund for that year if his demand was not honored.

$140,000,000, exclusive of interest, again asserting that North Carolina had unconstitutionally collected income tax on their federal pensions and military pay. Respondents asserted a number of affirmative defenses, including the defenses that the *Davis* case should be applied prospectively only and that Petitioners were barred by their failure to comply with N.C. Gen. Stat. § 105-267.

On October 3, 1990, the state trial court granted Petitioners' motion for summary judgment, allowing refunds for the Class A Petitioners for taxable years 1985-1988 and for the Class B Petitioners for taxable years 1986-1989. On appeal to the Supreme Court of North Carolina, Respondents raised seven issues including whether *Davis* should be applied prospectively only, whether *Davis* was even applicable to the National Guard tax benefit,[7] and whether Petitioners met the timely notice and payment under protest requirements of N.C. Gen. Stat. § 105-267.

On August 14, 1991, the Supreme Court of North Carolina reversed the trial court and held that Petitioners were not entitled to refunds because *Davis* should be applied prospectively only. *Swanson v. North Carolina (I)*, 329 N.C. 576, 407 S.E.2d 791 (1991). The Court

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[7] None of the Class B Petitioners were entitled to refunds on the additional and independent ground that the National Guard tax benefit did not constitute discriminatory taxation in violation of the Public Salary Tax Act or this Court's decision in *Davis*. *See* Argument II, *infra*, at pages 24-27.

granted Petitioner's rehearing request and reaffirmed its initial decision on December 6, 1991. *Swanson v. North Carolina (II)*, 330 N.C. 390, 410 S.E.2d 490 (1991).

This Court reviewed the decisions in *Swanson (I) and (II)* by writ of *certiorari* and reversed and remanded for reconsideration in light of *Harper v. Virginia Department of Taxation*, 509 U.S. ___, 113 S.Ct. 41, 125 L. Ed. 2d 74 (1993). *Swanson v. North Carolina*, 509 U.S. ___, 113 S. Ct. 3025, 125 L. Ed. 2d 713 (1993). On remand, the case was reargued after additional briefing. On March 4, 1994, the Supreme Court of North Carolina held in *Swanson III* that N.C. Gen. Stat. § 105-267 met the due process requirements enunciated in *McKesson v. Florida Division of Alcoholic Beverages and Tobacco*, 496 U.S. 18 (1990), and reiterated in *Harper* and dismissed Petitioners' refund claims for failure to comply with N.C. Gen. Stat. § 105-267. The present petition for writ of *certiorari* followed.

REASONS WHY THE WRIT SHOULD NOT BE GRANTED

This is not a proper case for allowing the writ of *certiorari* because the North Carolina Supreme Court correctly applied this Court's decisions in determining: (1) that the procedural requirements of N.C. Gen. Stat. § 105-267, including its timely notice and payment under protest provisions, fully satisfy due process standards, as enunciated in *McKesson* and reiterated in *Harper*; and (2) that Petitioners' failure to comply with these valid procedural requirements barred their refund claims. The

petition should not be allowed as to Class B Petitioners' refund claims for the additional reason that the former National Guard tax benefit did not constitute discriminatory taxation in violation of the Public Salary Tax Act or this Court's decision in *Davis*.

I. THE PETITION SHOULD BE DENIED BECAUSE THE NORTH CAROLINA SUPREME COURT CORRECTLY APPLIED THIS COURT'S DECISIONS IN *McKESSON* AND *HARPER* IN DETERMINING THAT PETITIONERS WERE NOT DEPRIVED OF DUE PROCESS WHEN THEIR REFUND CLAIMS WERE DENIED FOR FAILURE TO MEET THE PROCEDURAL REQUIREMENTS OF NORTH CAROLINA'S REFUND STATUTE, N.C. GEN. STAT. § 105-267.

1. N.C. Gen. Stat. § 105-267 met the requirements of due process by providing Petitioners with the opportunity to obtain meaningful backward-looking relief in the form of refund of taxes paid on their federal pension income in 1988.

N.C. Gen. Stat. § 105-267 forbids predeprivation challenges to the collection of a tax and provides instead for the refund of unlawful taxes to taxpayers who make timely refund demands. Years before *Davis* was decided the Supreme Court of North Carolina had held that N.C. Gen. Stat. § 105-267 is the exclusive method by which a taxpayer can challenge the constitutionality of a State

tax statute and obtain a refund. *Coca Cola v. Coble*, 293 N.C. 565, 238 S.E.2d 780 (1977). Taxpayers were on notice of both the statute and the *Coca-Cola* decision long before *Davis* was decided.

In *Swanson III* the Supreme Court of North Carolina rejected Petitioners' contention that they were deprived of due process when State officials denied their refund claims for failure to meet N.C. Gen. Stat. § 105-267's requirements:

> Plaintiffs [Petitioners before this Court] contend the statutory refund procedure transgresses the Due Process Clause of the Fourteenth Amendment of the United States Constitution insofar as it bars full refunds to plaintiffs for tax years 1985 through 1988 which, plaintiffs contend, are required by the United States Supreme Court's decision in *Harper v. Virginia Department of Taxation*, 509 U.S. ___, 125 L. Ed. 2d 74.
>
> We do not agree. Rather, we conclude that in light of both *Harper* and *McKesson Corporation v. Division of Alcoholic Beverage and Tobacco*, 496 U.S. 18, 110 L. Ed. 2d 17 (1990), the refund procedure provided in section 105-267 is free from any constitutional infirmity. It may, therefore, effectively bar actions for

> refunds in the tax years for which the procedure was not followed.

Swanson III, 335 N.C. at 684, 441 S.E.2d at 543.

Penetrating to the heart of the case, the North Carolina Supreme Court held that the timely notice and payment under protest provisions in N.C. Gen. Stat. § 105-267 were identical to those approved by this Court in *McKesson*:

> Plaintiffs contend, nevertheless, that the State cannot, consistent with due process, deprive them of full refunds of all taxes paid in all tax years within the period of the statute of limitations *even though these taxes were not duly challenged under the procedures established by section 105-267.* Again, *McKesson* answers this contention adversely to plaintiffs' position.
>
> *McKesson* holds that a state may provide full refunds to taxpayers, and at the same time, protect its fiscal stability by imposing "various procedural requirements on actions" seeking such remedies:
>
> > The State might, for example, provide by statute that refunds will be *available only to those taxpayers paying under protest or providing some timely notice of complaint*;

> execute any refunds on a reasonable installment basis; enforce relatively short statutes of limitations applicable to such actions
> . . . The State's ability in the future to invoke such procedural protections suffices to secure the State's interest in stable fiscal planning when weighed against its constitutional obligation to provide relief for an unlawful tax.

Id. at 45, 110 L. Ed. 2d at 41. Indeed, in remanding the case to the Florida Supreme Court, the United States Supreme Court noted, "upon remand the State may invoke as an independent basis for refusing to provide a refund, petitioner's failure to comply with a notice requirement that was in effect at the time of petitioner's tax payments." *Id.* at 24 n.4, 110 L. Ed. 2d at 28 n.4.

North Carolina thus gives taxpayers desiring to challenge the illegality, or unconstitutionality, of a tax a clear and certain remedy and meaningful, backward-looking relief by providing a full refund of the tax if the challenge is successful. It also provides a clear and fair opportunity to contest the tax by the procedures set out in section 105-267. Denial of refunds to

> taxpayers for the tax years for which they failed to comply with this procedure does not, as the Court made clear in *McKesson*, deprive these taxpayers of constitutional due process.

Swanson III, 335 N.C. at 686-87, 441 S.E.2d at 544-45. (Emphasis added).

The Supreme Court of North Carolina rejected Petitioners' argument that *Harper* had somehow modified *McKesson*. *Swanson III*, 335 N.C. at 688, 441 S.E.2d at 545-46. It determined that "[t]he *Harper* Court did not fashion a new test for due process. Instead, it relied on well-established tests enunciated in *McKesson* and earlier cases." *Swanson III*, 335 N.C. at 689, 441 S.E.2d at 546:

> Thus, *Harper* did not modify the Court's previous jurisprudence, including *McKesson*, regarding the tests for determining whether a state's postdeprivation remedy by which a tax may be challenged on legal or constitutional grounds satisfies due process. Rather, the *Harper* Court made it clear that a state satisfied due process if it offered taxpayers relief consistent with the due process standards delineated in *McKesson*.

Swanson III, 335 N.C. at 691, 441 S.E.2d at 547.

The Supreme Court of North Carolina was plainly correct in holding, based on *McKesson*, that N.C. Gen. Stat. § 105-267, both on its face and as applied to Petitioners' claims, met the requirements of due process. *McKesson* expressly held that the Due Process Clause does *not* require a predeprivation remedy for unconstitutional taxation and that states may fully satisfy their due process obligations to taxpayers by providing "a meaningful *opportunity* to secure postpayment relief for taxes already paid pursuant to a tax scheme ultimately found unconstitutional." *McKesson*, 496 U.S. at 22. (Emphasis added). In *McKesson*, the Court further expressly held that states may constitutionally protect their financial security by limiting taxpayers' opportunities for refunds of taxes collected pursuant to a statute later held unconstitutional to those taxpayers who comply with procedural requirements such as timely notice and payment under protest.

McKesson draws upon a long line of cases holding that the Due Process Clause calls for a balancing of the interests of citizens and government. *See, e.g., Matthews v. Eldridge*, 424 U.S. 319 (1976). The Court has consistently recognized that where the state's interest is one of overriding significance, citizens may be deprived of property without a prior hearing. Tax collection is such an area. *See, e.g., Bob Jones University v. Simon*, 416 U.S. 725 (1974); *Phillips v. Commissioner*, 283 U.S. 589, 595-97 (1931); *Dodge v. Osborn*, 240 U.S. 118 (1916); *see also*, Lawrence H. Tribe, *American Constitutional Law*, § 10-14 at 720-21 (2d ed., 1988). Balancing the interests of taxpayers and the government,

the Court held that states may adopt postpayment remedies because "[a]llowing taxpayers to litigate their tax liabilities prior to payment might threaten a government's financial security, both by creating unpredictable interim revenue shortfalls against which the State cannot easily prepare, and by making the ultimate collection of validly imposed taxes more difficult." *McKesson*, 496 U.S. at 36-37. The Court reiterated that "States may avail themselves of a variety of procedural protections against any disruptive effects of a tax scheme's invalidation, such as providing by statute that refunds will be available to only those taxpayers paying under protest, or enforcing relatively short statutes of limitation applicable to refund actions . . . . Such procedural measures would sufficiently protect States' fiscal security when weighed against their obligation to provide meaningful relief for their unconstitutional taxation." *McKesson*, 496 U.S. at 50.

This Court's holding in *McKesson* is clear and unambiguous: statutory preconditions to obtaining refunds, such as timely notice and payment under protest, do not deny due process and are constitutional. *Harper* in no way changes this result. North Carolina's refund statute, N.C. Gen. Stat. § 105-267, incorporates the very procedural safeguards this Court expressly approved in *McKesson*. Thus, the Supreme Court of North Carolina correctly applied *Harper* and *McKesson* in holding that N.C. Gen. Stat. § 105-267 is constitutional.

Petitioners nevertheless persist in portraying themselves as victims of an unfair application of N.C. Gen. Stat. § 105-267. They first contend that giving timely notice and paying under protest would have been futile because the Department of Revenue lacked the power to declare a State tax statute unconstitutional. Petitioners overlook the facts. Within days of the *Davis* decision, Department of Revenue officials sought and received the advice of counsel and later, based on the Supremacy Clause of the United States Constitution and this Court's decision in *Davis*, *made refunds* totalling over $9,000,000 to more than 12,000 federal pensioners who met the requirements of N.C. Gen. Stat. § 105-267.

Second, petitioners argue that the timely notice and payment under protest provisions of N.C. Gen. Stat. § 105-267 serve no valid purpose. As this very case illustrates, constitutional challenges can put a staggering amount of revenue at risk and can imperil the financial stability of a state and its ability to serve all of its citizens. As this Court observed in *McKesson*, states must be able to protect public revenues intended for the benefit of all citizens. The 30-day refund demand requirement gives the State notice of potential claims upon public funds, and the 90-day delay provides the Department of Revenue a reasonably short period to pay meritorious claims and thereby avoid needless litigation. In the case of a demand not honored within 90 days, the taxpayer can immediately present any constitutional challenge he may have to the Superior Court. N.C. Gen. Stat. § 105-267's requirements afford the State some measure of fiscal protection while assuring taxpay-

ers ready access to a court of competent jurisdiction to adjudicate constitutional claims. *Cf. Rosewell v. LaSalle National Bank*, 450 U.S. 503 (1981). Petitioners are simply wrong in saying the requirements of N.C. Gen. Stat. § 105-267 serve no valid purpose.

Third, Petitioners claim that the Department of Revenue's bulletins and instruction pamphlets were "affirmatively misleading" because they discussed the three-year period for requesting the refund of an overpayment due to a computational error but failed to explain how to make a constitutional challenge under N.C. Gen. Stat. § 105-267. The Court of Appeals for the Fourth Circuit rejected this notion:

> Plaintiffs' argument that Powers "changed" the refund procedures relies substantially upon statements in income tax bulletins regarding the statute of limitations. *We find this reliance misplaced because the bulletins clearly state in their preface that they "do not cover all phases of the law."* In fact, only the refund procedures under Gen. Stat. § 105-266 for routine overpayments due to miscalculation are discussed; the bulletins do not mention Gen. Stat. § 105-267, which applies to refunds of unconstitutional taxes.

Powers, 937 F.2d at 972. (Emphasis added).

Unlike the Petitioners, the Court of Appeals recognized that these kinds of publications cannot, and need not, be all-inclusive. The purpose of these bulletins and pamphlets is to present general information having the greatest interest to the largest number of taxpayers. These publications were not intended to address exceptional circumstances. Rather, they were designed to answer the kind of questions the average taxpayer is likely to have as he fills out his return. Since computational errors are common and constitutional challenges are rare, it is entirely reasonable for tax instructions and bulletins to describe only the refund procedure for routine overpayments and to put the taxpayer on notice that the publications "do not cover all phases of the law."

Fourth, Petitioners contend that application of N.C. Gen. Stat. § 105-267's procedural requirements to their refund claims was an abrupt after-the-fact change in policy formulated to deprive them of refunds. The Court of Appeals in *Powers* found this argument implausible:

> The thirty-day period for requesting refunds of unauthorized taxes is set by statute, not by the whims of the Secretary of Revenue. *See* N.C. Gen. Stat. § 105-267 (1989). Payment of the tax followed by a request for a refund is the exclusive means for remedying an unconstitutional tax in North Carolina. *Coca-Cola*, 238 S.E.2d at 783. Furthermore, the statutory require-

> ment that taxpayers demand refunds of invalid taxes within thirty days of payment has been North Carolina law for approximately fifty years, which must have provided plaintiffs some minimum of notice.

Powers, 937 F.2d at 971.[8]

Fifth, Petitioners contend that the Supreme Court of North Carolina somehow deprived them of due process by holding that each member of a class of taxpayers challenging the validity of a tax must meet the timely notice and payment under protest provisions of N.C. Gen. Stat. § 105-267. *See Swanson III*, 335 N.C. at 680-83, 441 S.E.2d at 542-43. In North Carolina, a class action can be used to aggregate valid claims for litigation, but claims which have already expired as a matter of law for failure to preserve them cannot be resurrected by combining them or mixing them with valid claims. The Secretary of Revenue's refusal to accept Petitioners' class demands did not deny them due process. Her reply describing the kind of information needed to identify taxpayers with valid claims did not impose new conditions. It simply explained why Petitioners' collective demand for refunds was insufficient to separate valid individual claims from those that had expired. *Swanson III*, 335 N.C. at 682-83, 441

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[8] Predecessor statutes to N.C. Gen. Stat. § 105-267 date back to 1887. *See Kirkpatrick v. Currie*, 250 N.C. 213, 215, 108 S.E.2d 209, 210 (1959).

S.E.2d at 542-43. There was nothing unconstitutional about this.

Finally, Petitioners assert that by relying on N.C. Gen. Stat. § 105-267 North Carolina has in effect blocked retroactive application of *Davis*. To the contrary, North Carolina has simply protected its fiscal stability by using the very procedures this Court unanimously approved in *McKesson*. North Carolina has met and exceeded the due process requirements enunciated in *McKesson* and reiterated in *Harper* by providing refunds for those federal pensioners who complied with the procedural requirements of N.C. Gen. Stat. § 105-267 and by giving tax credits to those who did not. The Supreme Court of North Carolina correctly applied *Harper* and *McKesson* in *Swanson III*, and there is no need for this Court to review that decision by *certiorari*.

2. The Supreme Court of North Carolina correctly declined to give preclusive effect to a preliminary jurisdictional finding by the District Court in Petitioners' federal litigation.

Petitioners initially sued the Respondents in the United States District Court for the Eastern District of North Carolina in April 1989. Ruling on Respondents' motion to dismiss that action for lack of subject matter jurisdiction, Judge Malcolm H. Howard found that N.C. Gen. Stat. § 105-267, as applied to Petitioners' claims, was not a "plain, speedy and efficient" remedy within the meaning of the Tax Injunction Act, 28 U.S.C. § 1341. He then dismissed on Eleventh Amendment

grounds Petitioners' claims for monetary damages against all State officials except Secretary of Revenue Helen Powers, leaving only Petitioners' claims for prospective declaratory and injunctive relief.

Secretary Powers appealed, and the Court of Appeals for the Fourth Circuit reversed, concluding that Powers was entitled to qualified immunity and that no claim lay against her in her individual capacity. *Powers, supra.* In its review of Secretary Powers' immunity claim, the Court of Appeals rejected arguments Judge Howard had relied upon in ruling on the Tax Injunction Act, thereby severely undermining his finding that N.C. Gen. Stat. § 105-267 was not a "plain, speedy and efficient" remedy as to Petitioners' claims. Following the reversal by the Court of Appeals, the federal case lay dormant for several years while Petitioners pursued their state court action.

After this Court's remand of *Swanson I and II* for reconsideration in light of *Harper* in June 1993, Petitioners moved the federal District Court for entry of judgment. They contended that the court's jurisdictional finding was binding upon Respondents and that *Harper* mandated refunds in the absence of a predeprivation remedy. They also told Judge Howard they wanted the judgment so they could demand that the Supreme Court of North Carolina give it *res judicata* effect in *Swanson III*. Respondents countered that the federal court docket entries indicated the case had been closed without any final judgment, that the jurisdictional finding was not a decision on the merits of Petitioners' due process claims,

that Petitioners had misinterpreted *Harper* and *McKesson*, and that the Eleventh Amendment barred entry of a judgment designed to control the decision in *Swanson III*, then pending before the Supreme Court of North Carolina on remand from this Court. *See Green v. Mansour*, 474 U.S. 64 (1985); *Edelman v. Jordan*, 415 U.S. 651 (1974).

While their motion for entry of judgment in federal court was pending, Petitioners demanded that the Supreme Court of North Carolina give preclusive effect to Judge Howard's jurisdictional finding and asked that Court to enter judgment in their favor. In *Swanson III*, the Supreme Court of North Carolina declined, noting that "[i]n the federal case, by an order dated 26 October 1993, United States District Court Judge Malcolm H. Howard found that 'a final judgment has not been issued in this case. . . .'" *Swanson III*, 335 N.C. at 692, 441 S.E.2d at 548. Thus, there was no basis to require the North Carolina Supreme Court to give the jurisdictional finding preclusive effect. This conclusion was later reinforced in Judge Howard's May 6, 1994 order granting summary judgment to Respondents in the federal action:

> This court's August 16, 1990, order was a finding for the purposes of jurisdiction under the Tax Injunction Act. It was *not* a determination that N.C. Gen. Stat. § 105-267 violated the due process clause. Plaintiffs litigated their due process claim in front of the state supreme court and

> lost. This court is required, as a matter of federal law, to give preclusive effect to a judgment of the North Carolina Supreme Court.

Judge Howard's Order, Petitioners' Appendix, at page A-85. (Emphasis added). Judge Howard was correct that the law compelled this result. *See Parson's Steel Inc. v. First Alabama Bank*, 474 U.S. 518 (1986); *Kremer v. Chemical Construction Corp.*, 456 U.S. 461 (1982).

Thus, the federal judge who made the Tax Injunction Act finding did not consider it to have sufficient finality for preclusive effect, and the Supreme Court of North Carolina agreed. There is no need for this Court to review the Supreme Court of North Carolina's decision on this point by *certiorari*.

II. AS TO CLASS B PLAINTIFFS' CLAIMS, THE PETITION SHOULD BE DENIED FOR THE ADDITIONAL REASON THAT THE FORMER STATUTORY INCOME TAX BENEFIT FOR NATIONAL GUARD MEMBERS WAS NOT DISCRIMINATORY TAXATION IN VIOLATION OF THE PUBLIC SALARY TAX ACT OR CONTRARY TO THIS COURT'S DECISION IN *DAVIS V. MICHIGAN DEPARTMENT OF TREASURY*.

Class B Petitioners claim that the former North Carolina National Guard tax benefit constituted discrimi-

natory taxation in violation of the Public Salary Tax Act and was contrary to this Court's decision in *Davis*. This contention is premised on a superficial application of the *Davis* decision and on the mistaken assumption that federal reservists and active duty military personnel were paid from the United States Treasury but that North Carolina National Guardsmen were paid from the State treasury. The two groups are actually compensated from the same source -- the United States Treasury. Thus, there was no discrimination against federal officers or employees based solely on the federal source of their compensation -- the underpinning of the Public Salary Tax Act and the intergovernmental tax immunity doctrine.

In *Perpich v. Department of Defense*, 496 U.S. 334 (1990), this Court traced the evolution of the National Guard and explained that since 1933 all persons serving in state national guard units have dual appointments, either by enlistment or commission, in both the state national guard and the National Guard of the United States. The Court noted that, "[t]he Federal Government provides virtually all of the funding, materiel, and leadership for the State Guard units." *Perpich*, 496 U.S. at 351. In North Carolina, State law provides for payment for national guard service from State funds *only* when members of the national guard are called into State service by the Governor to execute the laws, secure the safety of persons and property, suppress riots or insurrection, repel invasions or provide disaster relief. N.C. Gen. Stat. §§ 127A-16, -105 and -106. As the Court of Appeals for the Fourth Circuit noted, the

federal government in 1989 paid more than 99 per cent of the compensation for personal service disbursed to North Carolina National Guardsmen. *Powers*, 937 F.2d at 972-73.

The Public Salary Tax Act was enacted to authorize states to tax federal compensation as long as the state tax does not discriminate *based solely on the federal source of the compensation*. The critical determinant for intergovernmental tax immunity and Public Salary Tax Act analysis is the *source* of the compensation to be taxed. Since both the Class B Petitioners and members of the North Carolina National Guard were paid from the federal treasury, the tax benefits formerly accorded to North Carolina National Guardsmen did not discriminate against federal reservists or active duty military personnel based on the federal source of their pay. The *Davis* decision and the Public Salary Tax Act simply do not recognize claims of discrimination as between groups of federally compensated employees.[9]

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[9] Even assuming *arguendo* that the Public Salary Tax Act and the doctrine of intergovernmental tax immunity are somehow applicable, significant differences between the duties of the federal armed forces and North Carolina National Guard would nonetheless justify disparate treatment. *Davis*, 489 U.S. at 815-17. The tax benefit partly compensated State national guard soldiers for remaining available for State emergency service when called by the Governor -- an obligation over and above their federal military obligation and one not shared by federal reservists and active duty military

The Class B Petitioners have not suffered discrimination based on the federal source of their pay. The tax benefit formerly extended to North Carolina National Guardsmen did not violate the Public Salary Tax Act or the principles of intergovernmental tax immunity enunciated in *Davis*. Class B Petitioners' petition for a writ of *certiorari* should not be granted for this additional reason.

CONCLUSION

The petition should be denied. The North Carolina Supreme Court correctly applied this Court's decisions in determining that North Carolina's refund statute, N.C. Gen. Stat. § 105-267, met the requirements of due process as enunciated in this Court's unanimous decision in *McKesson* and reiterated in *Harper*. That Court also correctly determined that Petitioners' failure to meet the exclusive and longstanding procedural requirements of N.C. Gen. Stat. § 105-267 barred their refund claims. As to Class B Petitioners, the petition should be denied for the additional reason that the former National Guard tax benefit did not constitute discriminatory taxation in violation of the Public Salary Tax Act or this Court's decision in *Davis*.

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personnel. The national guard tax benefit also served to attract persons interested in the military reserves to choose the North Carolina National Guard.

Respectfully submitted, this the 23rd day of June, 1994.

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APPENDIX

CONTENTS OF APPENDIX

N.C. Gen. Stat. § 105-267 . . . . . 1a

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§ 105-267. Taxes to be paid; suits for recovery of taxes.

No court of this State shall entertain a suit of any kind brought for the purpose of preventing the collection of any tax imposed in this Subchapter. Whenever a person shall have a valid defense to the enforcement of the collection of a tax assessed or charged against him or his property, such person shall pay such tax to the proper officer, and such payment shall be without prejudice to any defense of rights he may have in the premises. At any time within 30 days after payment, the taxpayer may demand a refund of the tax paid in writing from the Secretary of Revenue and if the same shall not be refunded within 90 days thereafter, may sue the Secretary of Revenue in the courts of the State for the amount so demanded. Such suit may be brought in the Superior Court of Wake County, or in the county in which the taxpayer resides at any time within three years after the expiration of the 90-day period allowed for making the refund. If upon the trial it shall be determined that such a tax or any part thereof was levied or assessed for an illegal or unauthorized purpose, or was for any reason invalid or excessive, judgment shall be rendered therefor, with interest, and the same shall be collected as in other cases. The amount of taxes for which judgment shall be rendered in such action shall be refunded by the State; provided, nothing in this section shall be construed to conflict with or supersede the provisions of G.S. 105-241.2. (1939, c. 158, s. 936; 1955, c. 1350, s. 15; 1957, c. 1340, s. 10; 1977, c. 946, s. 1.)